

Internal Revenue Service

Department of the Treasury

District
Director

Person to Contact:

Telephone Number:

Refer Reply to:

Date:

JUN 27 1985

Gentlemen:

We have considered your application for exemption from Federal income tax as an organization described in section 501(c)(3) of the Internal Revenue Code of 1954.

The information submitted discloses that you were incorporated under the nonprofit corporation laws of the State of [REDACTED] on [REDACTED].

Your corporation's purpose is stated in Article TWO of its Articles of Incorporation. That provision reads, in part, as follows:

"The specific purposes for which this corporation is organized are: (1) to conduct studies which are intended to further knowledge and understanding in areas effecting public policy decisions; (2) to provide technical assistance and training to federal, state, and local public agencies; and, (3) to provide information which will enhance public awareness in designated subject areas."

Your corporation's activities and proposed activities are summarized in Form 1023 Part III 3. That summary reads, in part, as follows:

"Presently, [REDACTED] is two weeks into a grant awarded by the [REDACTED] to provide (as a non-profit organization) technical assistance and training to alcohol service programs to develop and improve the use of volunteers. The services are provided at no cost to the alcohol treatment programs, numbering up to [REDACTED] programs by [REDACTED]. The services are provided through a state grant; a copy of the budget and the full proposal accompanies this application package.

Proposed future activities are to provide services to public agencies to further enhance their service capability. These activities may consist of technical assistance, training, needs assessment and feasibility studies, and grant research."

From the information submitted, it appears that the services you provide are available from commercial sources. In Form 1023 Part III 5 you make the following statement:

"The staff [REDACTED] of the organization are current employees of [REDACTED], a for-profit corporation which conducts studies and manages projects related to evaluation, management, and training. All [REDACTED] work is contractual."

In a letter dated [REDACTED] we requested additional information about your operation so we could determine your proper tax exempt status. You responded to that request in a letter dated [REDACTED].

We asked if the grant you received from [REDACTED] covered all the costs connected with the services provided. You responded as follows:

"The grant from [REDACTED] covers all costs connected with the services provided by [REDACTED] per contractual agreement. The budget includes personnel, travel, office and equipment lease, supplies, telephone, photocopying, printing, and mail expenses for this project. Only costs associated with this specific project are covered in the grant provided by [REDACTED]."

We asked what you meant by the term "public agencies". You responded as follows:

"The term "public agencies" as used in Form 1023 Part III 3, refers to organizations not considered private enterprise. This includes public service non-profit groups (many of whom receive some funding from city, state, and federal government sources) and government agencies at the local, state and federal levels. At the present time, the majority of the organizations we serve are public service non-profit organizations."

We asked if you would sell consulting services to public agencies. We asked if your consulting fees would cover all the costs connected with the services provided. You responded as follows:

"Services performed by [REDACTED] will be supported by funding awards provided by local, state and federal government agencies, as well as private foundations (subject to [REDACTED]'s recognition as a tax-exempt organization by the Internal Revenue Service). Funds sought from public agencies will generally be received after the agency makes an award on the basis of selection from competitive bids submitted by non-profit applicants. It is anticipated that funding awards will cover, and not exceed, all expenses related to work promised in the application or proposal."

We asked you to state how many of the fourly alcohol treatment programs you contracted to provide services to were exempt from Federal income tax under section 501(c)(3). You responded as follows:

"In a telephone survey of these programs, only three were absolutely certain they were tax exempt under Internal Revenue Code 501(c)(3) per se."

Section 501(c) of the Internal Revenue Code of 1954 describes certain organizations exempt from income tax under section 501(a) and reads, in part, as follows:

"(3) Corporations, and any community chest, fund, or foundation organized and operated exclusively for religious, charitable, scientific, testing for public safety, literary, or educational purposes, or to foster national or international amateur sports competition (but only if no part of its activities involve the provision of athletic facilities or equipment), or for the prevention of cruelty to children or animals, no part of the net earnings of which inures to the benefit of any private shareholder or individual, no substantial part of the activities of which is carrying on propaganda, or otherwise attempting, to influence legislation, (except as otherwise provided in subsection (h)), and which does not participate in, or intervene in (including the publishing or distributing of statements), any political campaign on behalf of any candidate for public office."

Regs. 1.501(c)(3)-1(e)(1) provides that an organization may not be exempt under section 501(c)(3) if its primary purpose is the operation of a trade or business.

Section 162 defines the term "trade or business" to include any activity carried on for the production of income from the sale of goods or performance of services.

Generally, an organization that is primarily engaged in the sale of goods or services that are also available from commercial sources will not qualify for exemption under section 501(1)(3). It is the position of the Internal Revenue Service that such an organization is primarily engaged in the operation of a trade or business.

For example, Rev. Rul. 72-369, 1972-2 C.B.245 held that an organization that sold consulting services to unrelated tax exempt organizations was not entitled to exemption under section 501(1)(3). It was engaged in the operation of a trade or business.

In order to qualify for exemption under section 501(1)(3) an organization must show that it will not be in competition with commercial enterprises.

In B.S.W. Group, Inc., 70 TC 352Dec.35,175 the court held that an organization that engaged in the sale of consulting services to non-profit organizations was not entitled to exemption under section 501(c)(3). The organization in question failed to show that it would not be in competition with commercial entities. It was operating a trade or business.

In order to qualify for exemption under section 501(c)(3) an organization must show that its activities serve one or more of the purposes of that Code section. The purposes of a government unit are not necessarily the purposes of section 502(c)(3). The purposes of a public agency are not necessarily the purposes of section 501(c)(3). The purposes of a nonprofit organization are not necessarily the purposes of section 501(c)(3).

For example, in *Commissioner v Lake Forest, Inc.*, 305 F. 2d 814 (1962) the court held that an organization that operated a government supported cooperative housing project was not entitled to exemption from Federal income tax. The organization did not operate for the purposes of the code section under which it sought exemption.

An organization that donates services to other organizations described in section 501(c)(3) (or for such purposes) may itself qualify for exemption under that Code section.

Rev. Rul. 71-529, 1971-2 C.B. 234 held that an organization that donated services to other tax exempt organizations was entitled to exemption under section 501(c)(3).

From the information submitted it appears that you are primarily engaged in the sale of consulting services. It appears that similar services are available from commercial sources. It appears that you are in competition with commercial entities. Your services are available to a wide variety of organizations. Your activities do not necessarily serve the purposes of section 501(c)(3).

Your organization does not operate in a manner similar to the organization described in Rev. Rul. 71-529, 1971-2 C.B. 234. You do not donate services. You sell them on a contract basis for a fee designed to cover all your costs. You do not restrict your services to organizations described in section 501(c)(3) (or for such purposes).

Your organization is not entitled to exemption under section 501(c)(3) of the Internal Revenue Code of 1954 because your primary purpose is the operation of a trade or business and because you are not operated exclusively for the purposes of that code section.

You are required to file federal income tax returns annually, with your district director.

Contributions made to you are not deductible under section 170 of the Internal Revenue Code.

If you are in agreement with this proposed determination, we request that you sign and return the enclosed agreement Form 6018. Please note the instructions for signing on the reverse side of this form.

If you are not in agreement with this proposed determination, we recommend that you request a hearing with our office of Regional Director

of Appeals. Your request for a hearing should include a written appeal giving the facts, law, and any other information to support your position as explained in the enclosed Publication 892. You will then be contacted to arrange a date for a hearing. The hearing may be held at the office of Regional Director of Appeals or, if you request, at a mutually convenient District Office. A self-addressed envelope is enclosed.

If we do not hear from you within 30 days from the date of this letter, and you do not protest this proposed determination in a timely manner, it will be considered by the Internal Revenue Service as a failure to exhaust available administrative remedies and will then become our final determination. Section 7428(b)(2) of the Internal Revenue Code provides in part that, "A declaratory judgment or decree under this section shall not be issued in any proceeding unless the Tax Court, the Court of Claims, or the district court of the United States for the District of Columbia determines that the organization involved has exhausted administrative remedies available to it within the Internal Revenue Service."

Sincerely yours,

District Director

Enclosures:
Publication 892
Form 6018